

FILED

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SECOND DISTRICT COURT

**IN THE SECOND JUDICIAL DISTRICT COURT,
WEBER COUNTY, STATE OF UTAH, TAX DIVISION**

PACIFICORP, INC., et al.,
Petitioners,

vs.

UTAH STATE TAX COMMISSION,
Respondents.

**MEMORANDUM
DECISION AND ORDER**

Case No. 180903986 TX

Judge Noel S. Hyde

Pursuant to Utah Code Ann. § 59-1-601 et seq (2015),¹ this matter is before the Court for trial *de novo* from a final decision issued by the Utah State Tax Commission (the “Commission”). This Court is required to determine the fair market value of PacifiCorp’s Utah operating property as of the January 1, 2015, lien date. PacifiCorp contends that the value assessed by the Commission is excessive. The petitioning Counties contend that the value set by the Commission is too low. The Commission supports its prior determination of value.

The Court’s decision and valuation conclusion is organized as follows:

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¹ All references to the Utah Code are to the Code in effect on the January 1, 2015, lien date.

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I. OVERVIEW

A. Procedural History

On or about May 1, 2015, the Commission’s Property Tax Division (the “Division”) issued an assessment of PacifiCorp’s Utah operating property as of January 1, 2015, in which it asserted that the system value of PacifiCorp’s taxable, tangible operating property was \$13,900,000,000.² PacifiCorp filed a Petition for Redetermination, asserting a system value of \$12,675,000,000. The Utah counties (the “Counties”) where PacifiCorp operates also filed a Petition for Redetermination asking the Commission to increase the assessment.³

After conducting a formal hearing, the Commission issued its Findings of Fact, Conclusions of Law and Final Decision on May 23, 2018, which made an adjustment to the debt component in the capitalization rate used by the Division in its income approach. This adjustment increased the capitalization rate from 6.61% to 6.83% thereby reducing the system value for PacifiCorp’s taxable, operating properties to \$13,686,698,889. PacifiCorp believed that further adjustments should be made and filed a Petition for Judicial Review pursuant to Utah Code Ann. § 59-1-601. The Counties filed cross-petitions and joined in this appeal.

² “System value” or “unit value” means the total value of all of PacifiCorp’s property located in all of its states operating as one integrated unit. The Division allocated 41.76% (\$5,804,946,429) of the \$13,900,000,000 system value to Utah based on cost, revenue and other factors. The Division then made a reduction of \$19,326,293 for certain locally assessed property and the final estimated value for PacifiCorp’s property located in Utah was \$5,785,620,140. None of the parties dispute the Utah allocation factor or the method used to remove previously taxed property at the local level.

³ The Counties that filed the appeal of the original assessment as well as the appeal to this Court include: Beaver, Box Elder, Cache, Carbon, Daggett, Davis, Duchesne, Emery, Garfield, Grand, Iron, Kane, Millard, Morgan, Rich, Salt Lake, San Juan, Sanpete, Sevier, Summit, Tooele, Wasatch, Washington, and Weber.

B. Standard of Review

“The district court [has] jurisdiction to review by trial *de novo* all decisions issued by the [C]ommission.” Utah Code Ann. § 59-1-601. The Court must “make a new and independent assessment of property value without relying on or deferring to previous Commission assessments.” *T-Mobile USA, Inc. v. Utah State Tax Comm’n*, 2011 UT 28, ¶13, 254 P.3d 752. Because this is a *de novo* proceeding, this Court gives no deference to any prior assessments. *Id.* at ¶11.

In a *de novo* proceeding in a tax court, “a preponderance of the evidence shall suffice to sustain the burden of proof.” Utah Code Ann. § 59-1-604. “[W]hen a party chooses to bring a case to the tax court . . . the party’s only burden is to show by a preponderance of the evidence that its proposed valuation is more accurate than any other value.” *T-Mobile*, ¶17 (citations omitted). “The burden of proof shall fall upon the parties seeking affirmative relief and the burden of going forward with the evidence shall shift as in other civil litigation.” Utah Code Ann. § 59-1-604. Utah law gives the tax court “broad authority to devise its own remedy in a given case.” *T-Mobile*, ¶53.

C. Applicable Law

Utah law requires that “[a]ll tangible taxable property located within the state shall be assessed and taxed at a uniform and equal rate on the basis of its fair market value, as valued on January 1, unless otherwise provided by law.” Utah Code Ann. § 59-2-103 and *see* Utah Const. art. XIII, § 2(1). “Fair market value” is defined as “the amount at which property would change hands between a willing buyer and a willing seller, neither being under any compulsion to buy or sell and both having reasonable knowledge of the relevant facts.” Utah Code Ann. § 59-2-102(12).

The Commission is charged with the responsibility of annually determining the fair market value of the taxable properties of public utilities and properties that operate “as a unit across county lines, if the values must be apportioned among more than one county or state.” Utah Code Ann. § 59-2-201(1)(a)(i) and (ii). PacifiCorp is a public utility as defined by Utah’s Property Tax Act and it is undisputed that its properties are operated as a unit across state and county boundaries. Utah Code Ann. § 59-2-102 (31). Consequently, PacifiCorp’s operating properties should be valued as a unit operating together as one system, and then that unit value should be allocated to the respective states and apportioned to the respective counties within a particular state. *T-Mobile*, ¶35.

The parties agree that PacifiCorp’s operating properties should be valued using a unitary approach to determine the fair market value of that unit of operating properties. The parties have also agreed that 41.76% of PacifiCorp’s unitary system value should be allocated to the State of Utah.

“The Commission has adopted an administrative rule to provide internal guidance in unitary valuations. *See* Utah Admin. Code R884-24P-62 [Rule 62].” *Union Pacific Railroad Co. v. Utah State Tax Comm’n*, Case No. 090700830, 9 (Utah 2nd Dist. Ct. 2013). Although Rule 62 may provide guidance to this Court in evaluating appraisal methodologies, it is “not binding on this Court” and the Utah Supreme Court has recognized that “[r]equiring the tax court to use a specific valuation method ignores the reality that certain methodologies are not always accurate in every circumstance.” *Union Pacific Railroad*, at 8-9 (quoting *T-Mobile*, ¶51). Consequently, in this matter the Court has determined the fair market value of PacifiCorp’s taxable property by applying generally accepted valuation methodologies based upon the “weight of the credible evidence received.” *Id.* at 14.

II. ANALYSIS AND FACTUAL FINDINGS

The trial *de novo* began on Monday, September 16, 2019, and concluded on Monday, September 30, 2019. PacifiCorp was represented by Attorneys David J. Crapo and John T. Deeds. The Commission was represented by Attorneys Laron J. Lind, John C. McCarrey and Joshua R. Nelson. The Counties, except Salt Lake and Washington Counties, were represented by Attorney Thomas W. Peters. Salt Lake County was represented by Attorneys Timothy A. Bodily and LaShel Shaw. Washington County was represented by Attorneys Brian Graf, Eric Clarke and Natalie Nelson.

Because the primary issue to be decided by the Court is the correct valuation of PacifiCorp's taxable operating property, the strengths and weaknesses of the respective appraisers' valuation approaches were the focus of the testimony. The three parties submitted substantial and divergent evidence in support of their respective valuations. The Court heard testimony from fact and expert witnesses and evaluated and weighed the competency, completeness, consistency and reliability of their testimony. The Court found the expert witnesses that provided testimony during trial to be competent and credible in their identified areas of expertise, and notes that the divergence of opinions was most significantly attributable to the fact that a determination of "fair market value" is, to a large extent, an art form that defies absolute precision of computation. Subsequent to the trial, each party prepared and submitted proposed findings of fact and conclusions of law.

The Court has reviewed the parties' written submissions and has considered and weighed the testimony of all witnesses, together with the documentary evidence received. The Court, now being fully advised, makes the following factual findings and resolves the disputed issues

identified in the course of this proceeding, having concluded that these findings and conclusions are supported by a preponderance of the evidence:

1. The type of tax at issue in this matter is property tax.
2. The valuation lien date is January 1, 2015.
3. PacifiCorp is a vertically integrated, regulated electric utility, meaning that it generates electricity and also transmits that electricity to its retail customers. PacifiCorp owns tangible real and personal property that is subject to assessment in this matter.
4. PacifiCorp has retail customers in the States of Utah, Oregon, Wyoming, Washington, Idaho and California.
5. The three generally recognized approaches to value are the market approach, the cost approach, and the income approach. Each is discussed separately in this decision.

A. Market Approach

6. In the present case, based on the uniqueness of the subject property and the absence of substantial relevant data regarding “comparable sales,” neither the parties nor their experts gave any significant consideration or weight to the market approach. Therefore, no further discussion of the market approach will be included in this decision.

B. Cost Approach

7. The cost approach to value was addressed by all parties in this case, and while there were minor variations in the components used by the various experts in determining the cost-approach valuations, the Court finds that such variations reflect the personal preferences of the individual experts and constitute somewhat separate paths leading to similar conclusions.

8. Because the results reached are so similar, the factual presentations and arguments relating to the cost approach do not justify a finding or conclusion that any one particular method, or the use of any particular component in the cost calculation, is more factually accurate or legally appropriate than any other.

9. Based upon all of the information and argument provided, and because the Court finds by a preponderance of the evidence that the cost valuation proposed by the Commission is sufficiently supported, the Court finds that the appropriate cost-approach valuation component is \$12,856,533,197.

C. Income Approach

10. The essence of the income approach to valuation is the calculation of an income stream and the capitalization of that income stream by an appropriately-determined discount rate.

11. The income stream to be capitalized in this case is not in substantial dispute, and the Court, by a preponderance of the evidence, finds it to be \$1,020,000,000.

12. The determination of the appropriate capitalization rate was the principal focus of the evidentiary presentation and argument in this case.

13. Various models, including the internal components and factors of those models, were the subject of extensive, and frequently conflicting, expert testimony.

14. Notwithstanding the frequent expressions of differing expert opinions, the Court finds that the expressed disagreements reflect sincerely held and rationally based expert determinations of issues on which reasonable minds may, and in this case do, differ. Such differences do not, however, establish that the approach of any particular expert is necessarily superior or inferior to any other.

15. The factors addressed by all parties and experts in determining the appropriate discount rate include the cost of debt, cost of equity and the capital structure of the business to be applied to such cost components.

16. Regarding the determination of the cost of debt, there is very little actual difference in the effective cost of debt among the various parties. The Court finds that the market debt rate of 4.5% is appropriate. It is the debt rate determined to be acceptable by Mr. Tegarden, Mr. Brownell, and Mr. Hendrickson (absent the restrictions of Rule 62), and is not much different than the 4.74% proposed by Mr. Eyre.

17. Regarding the cost-of-equity component, the Court finds by a preponderance of the evidence that the Commission's cost of equity of 8.39% is better supported than the factor suggested by either Pacificorp or the Counties (their proposed factors being, respectively, 9.6% and 8.0%), and that it is the appropriate cost-of-equity factor to use in this case.

18. Authorized returns on equity are neither correlated to nor determinative of the calculation of the cost of equity for valuation purposes. The cost-of-equity rates calculated in rate cases serve the regulatory purpose of setting rates, but are not appropriate to establish value in a long-term perpetuity cash flow model.

19. A legal issue before the Court in this proceeding is whether Utah law requires the tax court to apply the preferred appraisal methodologies identified in Rule 62 in determining the Utah taxable value of PacifiCorp's operating property. The Court concludes it is not bound by Rule-62-preferred methodologies for two reasons. First, the rule itself does not require strict application of the preferred methodologies, but simply gives them a "rebuttable presumption." Second, applicable case law confirms that the tax court is not required to blindly follow Rule 62 in determining value. However, based upon all the evidence presented, the Court finds that the

methodologies and weighting set forth in Rule 62 regarding the determination of the cost-of-equity factor are appropriate in this case.

20. The Court further finds that neither PacifiCorp nor the Counties have demonstrated by a preponderance of evidence that other generally accepted appraisal methods for calculating the cost of equity result in a more accurate estimate of the fair market value of PacifiCorp's operating property than those used and relied on by the Commission in its cost-of-equity determinations.

21. Because the appraisers agree that market measures of debt, equity and capital structure should be used, when available, to develop a weighted average cost of capital ("WACC"), the Court finds that a market-based capital structure of 40% debt and 60% equity is supported by a preponderance of the evidence and appropriate in this case.

22. The discount rate, or WACC, is therefore calculated as follows:

Debt Rate	4.50 % x 40% =	1.80%
<u>Equity Rate</u>	<u>8.39% x 60% =</u>	<u>5.03%</u>
WACC		6.83%

23. Applying the indicated discount rate of 6.83% to the indicated income stream of \$1,020,000,000, the Court finds that the appropriate non-adjusted income-approach-to-value component is \$14,934,114,202.00. Subtracting the value of exempt intangible property, which the Court finds the Commission appropriately determined to be \$417,249,621.00, the Court finds the final income-indicator value to be \$14,516,864,581.00.

D. Weighting of Valuation Approaches

24. None of the valuation experts prepared a market-approach valuation, and thus no weight was given by the appraisers or by the Court to that approach. In its determination below, the Commission had weighted its cost approach and income approach indicators each at 50%. Mr. Hendrickson explained that he had considered the strengths and weaknesses of each indicator and the fact that this was how the Division had historically weighted the indicators for Pacificorp. Mr. Tegarden and Mr. Eyre argued for weighting the income approach higher. In Mr. Tegarden's case, because his income approach was lower than his cost approach, greater weighting on the income approach reduces value. The opposite is true for Mr. Eyre.

25. None of the appraisers presented a theoretical structure or formulaic approach to support their stated weighting preferences, and the Court notes that as the value determinations from the compared approaches converge, the impact of any weighting diminishes. It appears to the Court in this case that the disparate weighting suggestions were intended simply to drive the ultimate value determination either up or down, and that they are not supported by any calculable methodology based on the evidence presented. As a result, the Court finds that the 50/50 weighting used historically and recommended by the Commission is appropriate.

III. CONCLUSION

26. Consistent with the foregoing analysis, the Court finds that the unit value of the operating plant and assets of Pacificorp, Inc., in the State of Utah as of the lien date of January 1, 2015, is \$13,686,698,889.00. A summary of the Court's determinations as to the various components of the calculation of the unit value of Pacificorp Inc., is as follows:

Cost Approach			\$12,856,533,197.00
	NOI	\$ 1,020,000,000.00	
	Cost of Debt	4.50%	
	Cost of Equity	8.39%	
	Capital Structure (Debt/Equity)	40%/60%	
	Discount Rate (Cost of Capital)	6.83%	
	Gross Income Approach	\$14,934,114,202.00	
	Less Exempt Intangible Property	\$ (417,249,621.00)	
Net Income Approach			\$14,516,864,581.00
Weighting (Cost/Income)			50%/50%
System Value			\$13,686,698,889.00

27. There was no dispute in this matter regarding the Utah allocation percentage, which the Commission calculated to be 41.76%. Applying this to the value of \$13,686,698,889.00 results in a Utah value before final adjustments of \$5,715,565,456.00. There was also no dispute over the Commission's adjustment for vehicles and other property that had been locally assessed, which adjustment is found by the Court to be \$19,029,723.00. Subtracting this from the Utah value results in a final Utah assessed value as of January 1, 2015, of \$5,696,535,700.00.

28. Because the determination of this Court is consistent with the determination of the Commission below, and because no Petitioner has established by a preponderance of the evidence that any other suggested value more accurately reflects the fair market value of the subject property, the Court hereby

ORDERS, ADJUDGES, and DECREES that the previous determination of the Commission is sustained. This is the final determination of the Court on the issues presented, and no further documentation of the Court's order is required.

Dated this 23rd day of January, 2020.



Noel S. Hyde
District Court Judge

CERTIFICATE OF MAILING

I hereby certify that on the 24th day of January, 2020, I mailed a true and correct copy of the foregoing Memorandum Decision and Order as follows:

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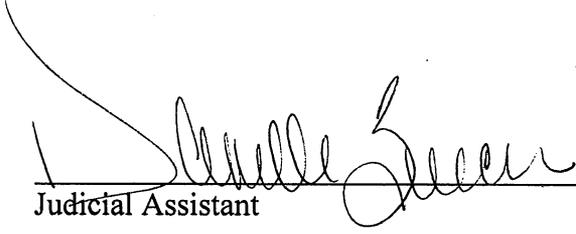
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